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June 26, 2007

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JUN 26 2007

Federal Communications Commission
Office of the Secretary

Ms. Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, SW
Portals II, Room TW-A325
Washington, DC 20554

Re: **REQUEST FOR TREATMENT AS TIMELY FILED**
High-Cost Universal Service Support, WC Docket No. 05-337;
Federal-State Joint Board on Universal Service, CC Docket No. 96-45.

Dear Ms. Dortch:

I am enclosing an original and four copies of the Reply Comments of Embarq Corporation in the above-referenced matter. Please accept these copies as timely filed under Commission rules, including 47 C.F.R. §§ 1.4, 1.46, 1.415, and any other sections that may apply. The filing deadline was 11:59 p.m. June 21, 2007.

I made several attempts to file the enclosed document electronically before the deadline, yet they were unsuccessful. Perhaps, ECFS was not operating as it should for some time before the deadline. Ultimately, I delivered copies of these Reply Comments to ECFS, the ECFS help desk, and William Caton in the Secretary's office at 11:45 pm. In compliance with the Commission's rules, I also filed by e-mail at that time with the parties listed on the Public Notice, Best Copy and Antoinette Stevens. In the message, I also requested guidance as to any further steps that may be necessary to file these Reply Comments.

Please call me at (202) 393-7113, or send me an e-mail message at jeffrey.s.lanning@embarq.com if you have any questions or need anything else.

Sincerely,

Jeffrey S Lanning

Jeffrey S Lanning
Director – Federal Regulatory

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	

EMBARQ REPLY COMMENTS ON THE NOTICE OF PROPOSED RULEMAKING (REGARDING THE RECOMMENDED DECISION OF AN INTERIM CAP ON HIGH COST SUPPORT FOR COMPETITIVE ELIGIBLE TELECOMMUNICATIONS CARRIERS)

Embarq Corporation (Embarq), on behalf of its local operating companies and interexchange and wireless operations, reiterates its support for the Recommended Decision of the Federal State Joint Board on Universal Service. The Joint Board has correctly and convincingly concluded that at least two federal universal service fund (USF) policies are deeply flawed: (1) using the high-cost support programs to promote competition, which results in duplicative funding to multiple carriers in areas where the market would not support even one; and (2) providing support to all eligible telecommunications carriers (ETCs) in each area based on the costs incurred by the incumbent local exchange carrier (ILEC) even though only the ILEC incurs the regulatory obligations that produced many of those costs.[1] Acting on this determination, the Joint Board has recommended that the Commission "stop the bleeding" while it develops a long-term solution to these failed policies. The recommended interim cap (Proposed Cap) on high-cost support for competitive eligible telecommunications carriers (CETCs) would be a legal, and effective temporary measure to facilitate fundamental reform.

[1] The Joint Board is also considering the different, yet equally important structural problem created by the policy of study-area averaging, which fails to recognize the true need for support in high-cost areas served by some carriers. That problem does not avail itself of an interim measure, however, to stop the harm while the Joint Board develops a long-term solution.

The Proposed Cap was nearly unanimously supported by the Joint Board, and it is widely supported among the parties to this proceeding, including state commissions and consumer groups.[2] As might be expected, however, CETCs that benefit from the current, failed policies object to the proposed interim solution. In essence, they argue that the Commission must allow the bleeding to continue even as the Joint Board works on long-term fundamental reform that will do away with duplicative support and the so-called "identical support" rule. This proposition makes no sense because the Commission is duty-bound to stop public interest harms—it should not allow failed USF policies to persist and further harm the public interest. Therefore, the Commission should implement the recommended interim cap, provided that the cap is temporary as the Joint Board has promised.

In an effort to bolster their objection to the proposed cap, CETCs make several claims. Most notably, they claim that the Proposed Cap will violate the principal of competitive neutrality because it will apply only to CETCs.[3] Instead, the Proposed Cap actually increases competitive neutrality because other ETCs also faced sector-specific caps and, in any event, CETCs don't incur comparable service obligations.

CETCs also claim that they should be permitted to continue growing their USF support because they put the funds to good uses.[4] In practice, however, it appears that USF support has had little impact on CETC coverage or choice. Moreover, where CETCs have increased coverage the results sometimes are utterly inconsistent with the goals of the USF. For example,

[2] *E.g.*, Comments of the People of the State of California and the California Public Utilities Commission; Comments of National Association of State Utility Consumer Advocates ("NASUCA"); and Comments of New York State Department of Public Service.

[3] *E.g.*, Comments of US Cellular and the Rural Cellular Association, at 24-37.

[4] *E.g.*, Comments of CTIA-The Cellular Association, at 6-10.

as discussed below,[5] Alltel appears to claim that it used USF support to build-out its network in Charlotte, North Carolina, which is the largest city in the state, and one of the forty largest metropolitan areas in the United States.

Finally, CETCs argue that the support they from USF should equal contributions from CETCs or commercial mobile radio service (CMRS) carriers.[6] This fundamentally misconstrues the purpose of USF because USF is designed to ensure that covered services are provided in places where it would not be economically rationally to provide such services in the absence of support. Accordingly, USF contributions will tend to flow from lower-cost areas to higher-cost areas. CETCs are free to build their networks where they choose, however, so one should not expect that they will be found predominately in lower-cost areas. Therefore, it is unlikely that CETC receipt of USF will match CETC support unless and until CETCs face the same build-out requirements and carrier of last resort obligations that are imposed on ILECs.

The Commission should not be misled by CETC arguments against the Joint Board Recommended Decision. Instead, the Commission should recognize that: (1) the Proposed Cap is an important step that will facilitate fundamental reform; (2) the Proposed Cap actually improves competitive neutrality; (3) CETCs are not generally using USF support to promote universal service; and (4) some modifications to the Proposed Cap may be sensible.

I. THE PROPOSED CAP IS AN IMPORTANT STEP THAT WILL FACILITATE FUNDAMENTAL REFORM.

The first step to fixing the USF structural flaws is to prevent further harm, and to do so sooner rather than later. The current growth in support, particularly support to create

[5] *Infra*, at 8.

[6] *E.g.*, Comments of Chinook Wireless.

competition in areas where it is uneconomic for a single provider to offer service, harms consumers and investment. As the first phase of a two-phase plan, the Proposed Cap would accomplish the important goal of immediately eliminating any additional upward pressure on the end-user USF assessment. The Commission requires market stability while it studies where and how to best allocate USF support to the high-cost areas that most need it. The implementation of the Proposed Cap is logical because it is imperative that the Joint Board and the Commission address the underlying structural problems that are inherent in the current USF system. The Proposed Cap will provide the Joint Board and Commission with the necessary stability and time needed to accomplish this structural reform in a manner that ensures the ongoing sufficiency, specificity and predictability of High-Cost Support.

II. THE PROPOSED CAP ACTUALLY IMPROVES COMPETITIVE NEUTRALITY.

As Embarq explained in its Comments, the Proposed Cap actually improves competitive neutrality. Embarq agrees with Verizon that "universal service caps are neither new nor novel."[7] Whereas the Rural High-Cost Loop Fund is capped for ETCs, high-cost loop support for CETCs is free to grow without limitation. Moreover, other USF programs are also capped. In brief, the Proposed Cap is not unique in that it is a cap on overall support; nor is it unique in that it is specific to one class of recipients. Rather, it is a responsible action narrowly tailored to the specific problem the Joint Board and Commission have chosen to address—substantial increases in USF support driven by duplicative support based on the identical support rule.

Perhaps more significantly, current CETC support itself violates the competitive neutrality principle. CETCs do not face the same obligations as ETCs, most importantly in that they are free to choose where and when to build their networks, and how much to charge for

[7] Comments of Verizon and Verizon Wireless, at 6.

their services. They are compensated, however, at the same levels as ETCs despite the fact that they do not have to build where it is not economically feasible to do so. In this way, the identical support rule is very clearly competitively biased and must be eliminated. Therefore, the public interest is served by capping support to CETCs immediately while the Joint Board and Commission work on fundamental reform that will address the current problems with USF, including the lack of competitive neutrality.

CETC use of high-cost support also violates competitive neutrality, because CETCs generally serve areas that already have multiple providers. Therefore, they divert USF support away from its intended use—bringing telecommunications service to places where it would not otherwise be available. Instead, they use USF support to bolster their competitive position or perhaps modestly increase coverage in areas where customers already have telecommunications service. This is directly contrary to the principle of universal service, and the mandates of the Communications Act. That support should be used instead to support carriers offering services where it is not economically feasible to build network facilities and provide service.

The current problem of competitive dis-parity with CETC support is compounded by the fact that CETCs often engage in "cream skimming." In its decision on the *Virginia Cellular ETC Petition*[8] and its decision on the *Highland Cellular ETC Petition*,[9] the Commission offered extensive discussions of the potential for cream-skimming in rural areas. The Commission also suggested that concerns regarding potential cream-skimming should factor into the public

[8] *Federal-State Joint Board on Universal Service Virginia Cellular, LLC Petition for Designation as an ETC in the Commonwealth of Virginia*, CC Docket No. 96-45, Memorandum Opinion & Order, 19 FCC Rcd 1563, ____ ¶¶ 31-35 (2004) (*Virginia Cellular*).

[9] *Federal- State Joint Board on Universal Service/Highland Cellular, Inc. Petition for Designation as an Eligible Telecommunications Carrier in the Commonwealth of Virginia*, CC Docket No. 96-45, Order, 19 FCC Rcd 6422, ____ ¶¶ 26-33 (2004) (*Highland Cellular*).

interest analysis of a petition for ETC designation in rural carriers' areas. In those orders the Commission stated that cream-skimming "occurs when competitors seek to serve only the low-cost, high-revenue customers in a rural telephone company's study area."[10] When he was a Commissioner, Chairman Martin explained that CETCs currently can engage in cream skimming in violation of the competitive neutrality principle. In the Commission's decision adopting some controls on CETC use of high-cost support, he wrote that he would prefer that:

> the Commission require ETCs to provide service throughout the same geographic service area in order to receive universal service support. This obligation would help guard against the potential for creamskimming. I would have supported a recommendation to deny future requests to redefine the service areas of incumbent rural telephone companies--and to deny ETC designations in instances where an ETC's proposed service area does not cover the entire service area of the incumbent service provider.[11]

Commissioner Martin was right then, and he is right now to support the Proposed Cap. Many, perhaps most, CETCs seek study area waivers and avoid building in some high-cost areas served by the ETCs on whom their support is based. Others may use resale selectively to avoid serving the highest-cost areas. In both cases, CETCs are cream skimming by taking support based on ETC costs while avoiding serving the highest-cost areas that produced those support amounts.

[10] This definition of cream skimming is incomplete. The Commission's discussions of cream skimming in *Virginia Cellular* and *Highland Cellular* are limited to examinations of cream skimming across wire centers. The Commission did not address the very real problem of cream skimming within a single wire center. Moreover, the Commission did not asses the role that resale plays in facilitating cream-skimming by allowing the CETC to selectively avoid the actual cost of serving the highest-cost parts of supported areas while drawing support based on those costs. When these additional scenarios are also taken into account, it becomes clear that CETCs have, and likely take advantage of, many opportunities to cream skim by avoiding investments in the highest-cost areas while taking support based on the costs of the investments they avoid.

[11] Separate Statement of Commissioner Kevin J. Martin, Dissenting in Part, Concurring in Part, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Recommended Decision, 19 FCC Rcd 4257 ____ (2004) (*ETC Designation Recommended Decision Separate Statement*).

III. COMPETITIVE ELIGILBE TELECOMMUNICATIONS CARRIERS ARE NOT GENERALLY USING USF SUPPORT TO PROMOTE UNIVERSAL SERVICE.

Several CETCs claim that the Proposed Cap would harm consumers because they are putting USF support to good use, and in furtherance of the goals and purposes of universal service. It does not matter, however, whether CETCs do "good" things with USF support. Instead, they must use USF support to build networks where such networks would not otherwise exist. The evidence indicates that they do not. For example, Jeffrey Eisenach of Criterion Economics recently demonstrated that USF support does not appear to increase CETC service:

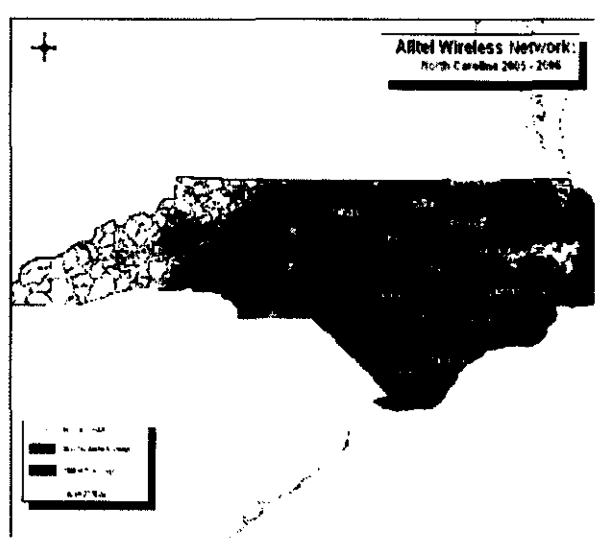
> The economic framework we present demonstrates that USF subsidies cannot affect relative prices of wireless service in rural areas, as wireless prices are set in national markets. Economic theory also suggests USF subsidies do not create strong incentives for wireless carriers to invest in rural areas, but theory alone cannot answer the question of whether there is nevertheless some effect. To resolve the issue, we develop and empirically test specific hypotheses regarding the relationship between USF subsidies and wireless availability and choice, and find no evidence of a positive relationship. This result holds with respect to both overall coverage (whether based on covered populations or covered land area), and with respect to measures of competition and choice.[12]

This conclusion supports very clearly the Joint Board decision to bar further increases in support to CETCs until it and the Commission can reform the system so that CETC support actually furthers the goals of USF.

Not only is there no correlation between USF support for CETCs and increased coverage, but it appears that CETCs use USF support to build or expand their networks in low-cost metropolitan areas that were never intended to receive high-cost support. One example may be

[12] Letter dated June 13, 2007 from Jeffrey Eisenach, Criterion Economics, to Marlene H. Dortch, FCC, *High Cost Universal Service Support*, WC Docket No. 05-337, at 42.

the following picture, which is the body of a slide Alltel presented to the Commission in this docket earlier this year.[13]



The slide is titled "Alltel's Use of ETC Funds" and the legend indicates that the blue areas represent Alltel's network as of the beginning of 2005 and the red areas represent Alltel's network at the end of 2006. The logical inference is that Alltel is saying that it used USF support to expand its network into the areas marked in red.

Alltel's apparent representation regarding its use of USF funds in North Carolina is interesting because one can see by referring to any map of the state that the red area roughly encompasses the North Carolina part of the *Charlotte* metropolitan area, including the city itself. Charlotte is the largest city in the state, and the metropolitan area is one of the forty largest in the United States. Without regard to whether Alltel customers benefited from this deployment it cannot be disputed that USF support was never intended to facilitate service in major metropolitan areas such as Charlotte, North Carolina. Therefore, it appears that Alltel admits

[13] Letter dated January 12, 2007 from Mark Rubin, Alltel, to Marlene H. Dortch, FCC, *High Cost Universal Service Support*, WC Docket No. 05-337, at 26.

that it uses USF support for unintended purposes. This is indicative of a broader reality, which is that high-cost support to CETCs does not advance universal service but, rather, only facilitates CMRS competition in already-served areas.

IV. SOME MODIFICATIONS TO THE PROPOSED CAP MAY BE SENSIBLE.

Several parties propose that the Proposed Cap be modified to end on a defined, certain end date as opposed to ending a year after the Joint Board issues a Recommended Decision on fundamental reform.[14] Embarq believes the Joint Board will meet its deadline and issue a Recommended Decision in the fall of 2007. Therefore, Embarq does not feel that the Proposed Cap needs modification. Embarq does believe, however, that the Proposed Cap *must not* become permanent. Fundamental reform is essential and the opportunity to accomplish it must not be missed. Therefore, Embarq would not oppose a "date certain" expiration of the Proposed Cap.

Other parties propose several exceptions or "carve outs" for CETC high-cost support to continue outside the Proposed Cap.[15] Notably, Dial-Tone Services and GCI argue that they are providing universal service in areas that are not currently served by any carrier. Such exceptions may be sensible because the fit with the fundamental purpose of the USF by providing service where it would not otherwise exist. If the Commission adopts an exception for unserved areas, however, it is imperative that the exception apply to *all of* the caps on high-cost support, including the current caps on support to ILECs. For example, where an ILEC built new facilities to provide service in a currently unserved area, that ILEC should also be able to receive high-cost support above and beyond any USF cap. This result would be necessary to fulfill the public policy behind a cap exception for unserved areas, and to further competitive neutrality.

[14] *E.g.*, Comments of Alltel, at 21.

[15] *E.g.*, Comments of Dial-Tone Services; Comments of General Communication, Inc.

V. *CONCLUSION*

The Commission should recognize that: (1) the Proposed Cap is an important step that will facilitate fundamental reform; (2) the Proposed Cap actually improves competitive neutrality; (3) CETCs are not generally using USF support to promote universal service; and (4) some modifications to the Proposed Cap may be sensible.

Respectfully submitted,

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